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September 15, 2006

Mary L. Cottrell, Secretary
Department of Telecommunications and Energy
One South Station, 2nd Floor
Boston, MA 02110

Re: NSTAR Electric Company, D.T.E. 06-40

Dear Secretary Cottrell:

Enclosed for filing is the NSTAR Electric Reply Brief in the above-referenced case. Also enclosed is a Certificate of Service.

Thank you for your attention to this matter.

Sincerely,

Robert N. Werlin

Enclosures

cc: Joan Foster Evans, Hearing Officer
Service List

COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

Boston Edison Company, Cambridge Electric Light Company, Canal Electric Company and Commonwealth Electric Company d/b/a NSTAR Electric	)	D.T.E. 06-40

CERTIFICATE OF SERVICE

I certify that I have this day served the foregoing document upon the Department of Telecommunications and parties of record in accordance with the requirements of 220 C.M.R. 1.05 (Department's Rules of Practice and Procedures).

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Dated: September 15, 2006

COMMONWEALTH OF MASSACHUSETTS

DEPARTMENT OF TELECOMMUNICATIONS AND ENERGY

Boston Edison Company, Cambridge Electric Light Company, Canal Electric Company and Commonwealth Electric Company d/b/a NSTAR Electric	)))))	D.T.E. 06-40

REPLY BRIEF OF BOSTON EDISON COMPANY, CAMBRIDGE ELECTRIC LIGHT COMPANY, CANAL ELECTRIC COMPANY AND COMMONWEALTH ELECTRIC COMPANY

Respectfully Submitted,

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Dated: September 15, 2006

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REPLY BRIEF OF BOSTON EDISON COMPANY, CAMBRIDGE ELECTRIC LIGHT COMPANY, CANAL ELECTRIC COMPANY AND COMMONWEALTH ELECTRIC COMPANY

I. INTRODUCTION

Boston Edison Company ("Boston Edison"), Cambridge Electric Light Company ("Cambridge"), Canal Electric Company ("Canal") and Commonwealth Electric Company ("Commonwealth"; together, the "Companies") submit this Reply Brief to the Department of Telecommunications and Energy (the "Department"), relating to the proposed merger among and between the Companies to create a single electric company, NSTAR Electric Company ("NSTAR Electric"). This Reply Brief responds to the initial briefs filed in this proceeding by the following intervenors: (1) the Attorney General; (2) Cape Light Compact ("CLC");[1] (3) Massachusetts Institute of Technology/President and Fellows of Harvard College ("MIT/Harvard"); (4) the Retail Energy Supply

[1] In two instances, CLC references (and in one case appends to its initial brief) extra-record documents (see CLC Initial Brief at 13, n.8 and Attachment B). Neither document was properly made part of the record and must be ignored by the Department. Boston Gas Company, D.P.U. 88-67 (Phase II), at 6-7 (1989).

Association ("RESA"); and (5) The Energy Consortium ("TEC").[2]

As described below, the intervenors have raised numerous issues that are not relevant to whether the Companies have met the statutory standard for approval of this merger and/or have proposed that approval of the merger be conditioned on actions that are unrelated to the merger itself. This merger case cannot and should not be a vehicle for altering established Department policies, changing the terms of the Department-approved Settlement Agreement in D.T.E. 05-85 or litigating issues beyond the scope of this case. But most importantly, the Department must reject the attempts by some of the intervenors to alter the statutory standard for consideration of merger proposals.

Because many of the intervenors addressed similar issues, this Reply Brief is organized by subject matter. Each section will begin with a brief summary of the arguments put forward by the intervenors, followed by the Companies' response. As shown below, the Companies have demonstrated that the proposed merger meets the statutory standard of review, and should be approved as filed.

II. ARGUMENT

A. Certain Intervenors Have Distorted the Statutory Standard of Review.

On the surface, each of the intervenors seems to agree with the Companies that the standard of review for this case under G.L. c. 164, § 96 ("Section 96") is the "no net harm" standard as articulated by the Department in numerous cases (Attorney General

[2] Many of the issues raised by the intervenors in their initial briefs were addressed by the Companies in their Initial Brief, and will not be repeated at length in this Reply Brief. The Companies do not intend that their silence concerning any matter reflects agreement with the positions taken by the intervenors. The Companies reassert the positions and arguments made in their Initial Brief.

Initial Brief at 7-8; CLC Initial Brief at 3-4; MIT/Harvard Initial Brief at 2-3; RESA Initial Brief at 5; TEC Initial Brief at 2-5). But below the surface, several of the intervenors apply a much different standard in arguing that the Companies have failed to meet the statutory test.

These intervenors attempt to turn the standard on its head by transforming a "no net harm" standard into a "no losers" test, implying that the Companies must demonstrate that no individual customer or group of customers will ever be adversely affected by the limited rate consolidations resulting from the merger.[3] This is not, and could not be, the statutory standard, since it would effectively bar any merger between jurisdictional electric companies within Massachusetts.

Both CLC and MIT/Harvard argue that the merger should be denied because the Companies have failed to demonstrate that the consolidation of transmission and Basic Service rates will never result in higher rates for any group of customers (CLC Initial Brief at 6-14; MIT/Harvard Initial Brief at 14-16). Having established this straw-man standard, they go on to argue that the transmission and Basic Service rates in Cambridge (as argued by MIT/Harvard) and Commonwealth (as argued by CLC) might be higher in the future on a consolidated basis than they would have been if computed separately, depending on the highly speculative predictions regarding, inter alia, future Federal Energy Regulatory Commission ("FERC") ratemaking decisions. Although the Companies disagree that there should be any systematic, long-term differences in these

3 Distribution rates and transition charges will remain separate for the three service territories under the terms of paragraph 2.17 of the Settlement Agreement in D.T.E. 05-85 (NSTAR Electric Initial Brief at 11; Exh. NSTAR-CLV-1, at 11; Tr. 2, at 246-247).

rates, as described in Section II.B and Section II.C, infra, these arguments are inconsistent with the statutory standard.

Notably, the intervenors have not argued that the rate-consolidation proposals will increase the total level of costs paid in the aggregate by the Companies' customers; indeed, that is not the case because, overall, the same level of costs will be recovered by the Companies after the merger as before the merger. Moreover, even where the consolidation of rates could result in a higher rate for a group of customers (in comparison to what they would be charged if the merger did not occur), there will be a corresponding decrease in the rate level for other customers. By definition, any "customer harm" would be offset by an equal "customer benefit" and thus there could be no net harm to customers. See, e.g., KeySpan Energy Delivery New England/NSTAR Gas Company, D.T.E. 02-44, at 7 (2002).

If the intervenors' no-losers test were to be applied, no merger of jurisdictional electric companies would occur, since it would be impossible to guarantee that future blended transmission rates for the merged company, for example, would always be lower than the lowest of the individual transmission rates if the companies were to remain separate. The very nature of rate averaging inevitably has the potential of creating possible winners and losers, and the no-net-harm standard properly rejects the notion that no adverse rate impact to any customer is a prerequisite to a merger.

B. The Consolidation of Transmission Rates Meets the No-Net-Harm Standard.

As stated above, no party claims that the aggregate level of transmission costs to be collected from customers will change by virtue of the proposed merger. The total level of costs will continue to be determined by rates established by the FERC (Exh.

NSTAR-CLV-1, at 16; see also NSTAR Electric Initial Brief at 15-20 for a full description of FERC-approved transmission rates). Nonetheless, both CLC and MIT/Harvard argue that customers in the present Commonwealth and Cambridge service territories, respectively, will be harmed by consolidating rates.[4] Both sets of arguments are based on the impact of future congestion costs on the consolidated transmission rates (vs. the impact of future congestion costs that would have applied to separate companies).

As stated in Section II.A, supra, the consolidation of transmission rates[5] meets the no-net-harm standard because the aggregate level of costs will not change as a result of the merger. However, it should be noted that the comments about the Companies' alleged failure to produce forecasts of the relative levels of transmission costs are without merit. CLC criticizes the Companies for not presenting "detailed, substantial and credible evidence" on future congestion costs (CLC Initial Brief at 9). It then says "NSTAR could have found some way of estimating" them and has ignored the effect of congestion costs (id. at 10). But the Companies have not ignored the congestion costs. In fact, they have invested hundreds of millions of dollars on the 345 kilovolt ("kV") project and the Cambridge upgrades to eliminate transmission constraints and minimize

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4 TEC requests that the Companies "make clear that any approval of the merger in no way modifies the terms…" of the settlement approved by the Department in D.T.E. 03-118-A/D.T.E. 04-114-A, that requires certain credits to the transmission rates for customers of Cambridge and Commonwealth (TEC Initial Brief at 19). The Companies confirm that they remain bound by the terms of that settlement and approval of the merger will have no impact on implementation of its terms.

5 The consolidation of the FERC transmission rates will occur "naturally" at the consummation of the merger because Cambridge and Commonwealth will no longer exist and the merged Boston Edison, to be renamed NSTAR Electric Company, will be the remaining legal entity and be subject to its surviving FERC transmission tariff (Exh. DTE-4-6).

the congestion costs that are paid by their customers (Exh. MIT-1-7; MIT-2-12; DTE-2-11; RR-AG-4).

Moreover, the record shows that the cost differentials between service territories caused by congestion costs are likely to be reduced or eliminated by the removal of transmission constraints (Exh. NSTAR-CLC-1, at 14-15; Exh. CLC-1-15). The forecasts of such costs are highly speculative, dependent on a number of uncertain variables and impossible to predict into the future with any reasonable level of confidence (Exh. CLC-1-9). Accordingly, the criticisms of the Companies' analysis about future levels of congestion costs, or the inability to predict such costs in future years, are unwarranted and not relevant to whether the merger meets the no-net-harm standard. In reality, future congestion costs will be what they will be as a result of developments in the wholesale market and decisions made by FERC and ISO-NE, and the implementation of the merger in this proceeding will have absolutely no impact on such costs.

For these reasons, and those stated in Section II.A, supra, the consolidation of transmission rates meets the Section 96 standard for approval of the merger.

C. The Consolidation of Basic Service Rates Meets the No-Net-Harm Standard and Is Not Anticompetitive.

No intervenor contends that the proposal to consolidate Basic Service rates (including the Basic Service adder) for Boston Edison, Cambridge and Commonwealth will, in the aggregate, increase the costs paid by customers. In fact, there could be total costs reductions associated with the procurement of combined supplies for Basic Service (Exh. DTE-3-4). The consolidation of Basic Service rates thus meets the no-net-harm standard. Nonetheless, several intervenors argue that the consolidation of Basic Service rates should not be approved.

Several intervenors address the issue of whether averaging rates for customers of the Companies will result in higher rates for some customers (Attorney General Initial Brief at 14-16; CLC Initial Brief at 12-14).[6] The Attorney General complains that, because it will not be possible to ascertain the actual bill impacts resulting from the averaging process until after supplies have been procured, the consolidation of Basic Service rates should be delayed until those impacts can be evaluated (Attorney General Initial Brief at 16). CLC argues that the consolidation of Basic Service rates "may result" in increases in rates for customers in the Commonwealth service territory (CLC Initial Brief at 14). Both of these arguments should be rejected.

Although it is undisputed that the aggregate level of Basic Service rates will not increase, the record also demonstrates that any differences in rates between the existing service territories will not be significant (Exh. NSTAR-CLV-1, at 13; Exh. DTE-1-23; Tr. 3, at 310-312). As stated in the Companies' Initial Brief at 13-14:

> The difference in the costs between the NEMA and SEMA load zones is not significant and, with the new 345 kV transmission upgrades to be completed by Boston Edison, this differential is expected to be minimal and declining in the future (Exh. NSTAR-CLV-1, at 13-14). [footnote omitted] An analysis of the real-time locational marginal pricing on a monthly, load-weighted basis was performed for the historical calendar years 2004 and 2005 for the NEMA and SEMA regions and is shown in Exhibit NSTAR-CLV-4 (id. at 14). On an average, 12-monthly-load-weighted basis, NEMA's prices were higher than the SEMA's prices by only 1.5 percent and 3.7 percent, for the years 2004 and 2005, respectively (id.). A key reason for the differential is the existence of transmission constraints in the NEMA region (id.). This differential in pricing of power supplies between the two regions should decline considerably when

[6] CLC also repeats its objections to the manner in which the Department requires companies in Massachusetts to apply the Default Service Adjustment (CLC Initial Brief at 10-12). The merger proposal includes no change in the Companies' tariff provisions regarding the Default Service Adjustment or in the Department's procedures for collection. Accordingly, the issue is not properly before the Department in this proceeding, and no action can or should be taken by the Department in this case.

> Boston Edison's new 345 kV line between Stoughton and Boston is placed in service (id.). Indeed, the new 345 kV line will substantially increase the transmission capacity of the integrated network system in the NEMA zone, including the Greater Boston area, thereby reducing the transmission congestion constraints of importing power into NEMA (id.).

RESA and TEC also raise the specter that the consolidation of Basic Service rates will adversely affect competition for generation services in Massachusetts (RESA Initial Brief at 7-14; TEC Initial Brief at 16-18). As described below, the record contradicts their assertions, which are nothing more than attempts to overturn longstanding Department policy with regard to the pricing of Basic Service to customers.

Both RESA and TEC provide selective citations from the Department order in which it established its policy with regard to the pricing of Basic Service (id., citing D.T.E. 02-40-A). In that order, the Department established the policy of requiring that separate NEMA and SEMA zonal prices be offered for medium and large commercial and industrial customers. D.T.E. 02-40-A at 9-10 (2003). What RESA and TEC omitted was the text of the Department findings with regard to small commercial and residential customers:

> The introduction of zone-differentiated rates for residential and small C&I customers has potential for customer confusion, especially given the uncertainty as to what the magnitude of zonal price differences will be. Therefore, after taking into account the relative costs and benefits of establishing zone-differentiated default service prices, the Department directs BECo and MECo to establish a service territory-wide default service rate for the residential and small C&I customer classes, averaged across load zones. The Department intends to revisit this issue after experience is gained regarding CMS, in particular the differences that may arise in congestion costs among the various zones, and the development of competition for these customer classes.

D.T.E. 02-40-A at 11. Nothing in this merger proposal will alter the existing implementation of the Department's requirements. Zonal prices will continue to be provided to medium and large commercial and industrial customers, and small commercial and residential customers will continue to receive "blended" rates. This is not the appropriate forum for RESA and TEC to seek changes in Department policy on Basic Service rates (Tr. 1 at 89-90), which was established in a generic proceeding applicable to all companies in Massachusetts and should be reconsidered (if at all) in a similar proceeding. Moreover, the record in this case does not establish that the continuation of that policy will have an adverse impact on competition in the state (Tr. 1, at 95-98). The intervenors cite to no evidence on this record to suggest that there is any meaningful level of competition in the market for small commercial and residential customers.

The intervenors' stated concerns relate to the fact that the consolidation of Basic Service rates will, under Department policies, require that rates for small commercial and residential customers to continue to reflect a blending of rates averaged across the NEMA and SEMA load zones. As described above, historical cost differences between the NEMA and SEMA zones will be reduced, particularly as a result of the implementation of the 345 kV project, which will eliminate any material difference between separate and blended rates. If the rates are the same, the purported effect on competition will be non-existent. In addition, there is no evidence to suggest that rate differences between zones, even if they exist, will have any anti-competitive impact (Tr. 3, at 333-334, 422-423).

In summary, the consolidation of Basic Service rates in conjunction with the merger meets the no-net-harm standard. There will be no negative change for the medium and large commercial and industrial customers because they will continue to receive zonal prices.[7] The zonal averaging of rates for small commercial and residential customers could have a small impact, depending on the future zonal price differences, but the averaging process will not result in any net customer increase in the aggregate. The merger does nothing to alter the existing Department policy for pricing Basic Service, which was established generically by the Department. Finally, the Companies have demonstrated that there is no impact on competition resulting from the proposed merger.[8]

D. The Reclassification of Cambridge's 13.8 kV Facilities Meets the No-Net-Harm Standard.

As described in the Companies' Initial Brief, the classification of Cambridge's 13.8 kV facilities that are presently treated for ratemaking purposes as transmission plant are to be reclassified as distribution plant as part of the NSTAR Electric merger, in accordance with the terms of the Department-approved Settlement Agreement in D.T.E. 05-85 (NSTAR Electric Initial Brief at 20, citing Exh. NSTAR-CLV-1, at 20; Exh. DTE-1-19; Exh. DTE-4-4). As part of that reclassification, the recovery of costs is to be transferred from transmission to distribution rates (Settlement Agreement at ¶ 2.18). See NSTAR Electric Initial Brief at 20-26, for a discussion of the reclassification and

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7 As mentioned above, the potential exists for price reductions for all customers of Basic Service resulting from the larger procurement (Exh. DTE-3-4).

8 The intervenors' complaints on Basic Service pricing are with the Department's policies, not the NSTAR Electric merger. Nothing in this merger would prevent the Companies from implementing any future change in Department Basic Service pricing policies. If parties wish the Department to reconsider its existing policy, they should so petition the Department, and the Companies will be bound by the outcome of such a proceeding. As was the case in the initial generic proceeding, interested parties must be offered an opportunity to be heard. Only based on a complete record could the Department consider whether it is appropriate to make such a policy change. Even aside from policy issues, the Department would need to consider relevant factual and implementation matters. For example, before NSTAR Electric could implement a zonal pricing system for Boston Edison customers, it would have to determine how its billing system would need to be altered to accommodate such a change, and the Department would have to consider whether the costs associated with altering billing systems are warranted.

ratemaking proposal. Three general issues have been raised by intervenors relating to the reclassification. Each of these is addressed below.

1. The Reclassification and Rate Adjustments Must Be Made Upon Consummation of the Merger.

The Attorney General and TEC argue that the reclassification of Cambridge's 13.8 kV facilities is premature (Attorney General Initial Brief at 9-12; TEC Initial Brief at 4-6). The Attorney General claims that the reclassification is "premature" because the 13.8 kV facilities do not yet meet FERC's seven-part test to be classified as distribution plant (Attorney General Initial Brief at 9-11).[9] The Attorney General also asserts that, in accordance with the Settlement Agreement, the reclassification cannot take place until after the consummation of the merger and after a separate proceeding (id. at 12). The Attorney General claims that this merger case does not constitute that "separate proceeding" (id.). TEC's argument is based on the assertion that the reclassification should not be effective until the completion of all elements of the projects relating to the East Cambridge Substation and the second 115 kV line to the Putnam Street Substation (TEC Initial Brief at 4-6).

As acknowledged by the Attorney General, "FERC's seven part test does not include any precise requirements or a bright line test for the Department to use in determining the appropriate classification…" (Attorney General Initial Brief at 11). Despite this correct characterization of the test, and ignoring the record evidence, both

[9] The Attorney General also states that the request is premature because FERC has not yet determined a "…just and reasonable rate as part of their merger proceeding" (Attorney General Initial Brief at 9). This argument is misleading and, at best, not clear because the merger proceeding at FERC does not request FERC to make any findings as to any of the Companies' transmission rates, nor is such a request necessary.

the Attorney General and TEC have focused solely on the fact that a second, redundant line that will link the Putnam Street Substation and the East Cambridge Substations is not yet in place. Although the completion of the installation of the second 115 kV line could affect the determination of whether the second factor of the FERC seven-part test is met (i.e., whether the 13.8 kV facilities are "radial" in nature), this narrow view ignores the totality of the test (Exh. DTE-2-10). Moreover, as the record establishes, it turns out that, even without the completion of the second line, Cambridge's 13.8 kV facilities are radial in nature (Tr. 1, at 155-156).

As described in the Companies' Initial Brief, between 1997 and 2007 five of the seven factors relating to Cambridge's 13.8 kV facilities will have changed (NSTAR Electric Initial Brief at 21-24). Many system changes have already affected the radial nature of the 13.8 kV facilities (Tr. 1, at 42-43; Exh. DTE-2-10, Exh. DTE-2-11), and "…the addition of the East Cambridge Substation and the 115 kV lines supplying it provides a 115/13.8 kV distribution substation that will allow the old intra-ties to be used as radial distribution circuits" (Exh. DTE-2-10). This is admittedly a relevant element in the seven-part test, but not necessarily the determining factor. But more importantly, the record establishes that everything is in place at this time relating to the East Cambridge Substation project so that it will operate as a distribution substation, even without the second line. At the request of the Department, the Companies presented Amin Jessa, Manager of System Engineering for NSTAR Electric, to respond to questions regarding distribution and transmission operational and engineering issues (Tr. 1, at 148). The following colloquy between the Bench and Mr. Jessa clarified the issue:

> Q. You're saying that without the second 115-kV line and intra-tie lines, the Department should approve the reclassification because it meets the seven-factor test?
>
> A. [JESSA] What I'm saying is that the East Cambridge substation would operate or could operate as a distribution substation whether it has -- even though it doesn't have a second line. The only difference is that, because we don't have a second line, we cannot rely on it as a redundant source of power and that we would have to rely on the existing distribution infrastructure for redundancy. And that would only come into play if there was a need for it, and we would have to automate some breakers and relays so that, if we were to lose a 115-kV line, that the customers would not be without power. So it would have to be a different approach. But under normal operating conditions, those lines would still be radial, and therefore they could still be classified and meet all the seven-point tests, the way I see it.

(Tr. 1, at 155-156). Accordingly, the record unequivocally establishes that Cambridge's 13.8 kV facilities now meet the FERC seven-part test to be classified as distribution.

The Attorney General's argument that, under the terms of the Settlement Agreement, the reclassification of Cambridge's 13.8 kV facilities should occur at a later date uncertain (after the merger) and must be decided in yet another proceeding misstates the Settlement Agreement. The Settlement Agreement's provision for the reclassification immediately follows the sentence establishing the fact that "<u>[u]pon</u> consummation of the merger, the FERC transmission rates of Cambridge and Commonwealth will be subject to the new formula rate tariff of Boston Edison and their FERC transmission tariffs will be withdrawn" (Settlement Agreement at ¶ 2.18 (emphasis added)).

The reclassification language was necessary in this context because the Boston Edison transmission tariff has no provision for the recovery of 13.8 kV facilities, and if the merger occurred without reclassification, there would be no rate recovery for these facilities (Exh. DTE-2-12). If that were to occur, NSTAR Electric would be unconstitutionally deprived of a reasonable opportunity to earn a reasonable return on these assets.[10] The timing for the transfer was also addressed in Exhibit DTE-5-13:

> Under the terms of the Department-approved Settlement Agreement in D.T.E. 05-85, the reclassification of Cambridge's 13.8 kV facilities and corresponding transfer of rate recovery is contemplated to take place at the time of the merger. Moreover, the change in classification must be done at year-end because the FERC tariffs are annual rates based on year-end plant balances and other data from the annual FERC Form 1. Changing classification at any other time frame makes revenue requirement determinations more complex and likely impossible to perform without a tariff change. The 13.8 kV transfer must be done concurrently with the merger. Since there will be no separate Cambridge FERC Form 1 after the merger date, it would be impossible to perform the formula rate calculation without maintaining separate accounting records after the merger, which would undercut one of the main administrative benefits that the merger provides.

With respect to the Attorney General's argument regarding the meaning of "separate proceeding" referenced in the Settlement Agreement, it is clear that the phrase was meant to establish that the ratemaking details of the transfer of recovery to distribution rates was to be implemented in a case other than D.T.E. 05-85. As the Attorney General knows, the Settlement Agreement did not resolve all of the specifics of the ratemaking issue, and that, before the transfer would be implemented, there would be another proceeding in which parties (including the Attorney General) would have an opportunity to participate. There is no implication that the proceeding would be a "stand-alone" or single-issue case; only that there would be another proceeding, separate from D.T.E. 05-85. In fact, this

[10] Not surprisingly, NSTAR Electric would not consummate the merger if the transfer of rate recovery were not satisfactorily resolved (id.. Tr. 2, at 290).

merger case is that separate proceeding (Tr. 3, at 412).[11]

Thus, the arguments of the Attorney General and TEC regarding the timing of the reclassification of Cambridge's 13.8 kV facilities are without merit.

2. The Proposed Revenue-Neutral Ratemaking Proposal Is Reasonable and Meets the No-Net-Harm Standard.

The intervenors do not challenge the Companies' right under the terms of the Settlement Agreement in D.T.E. 05-85 to transfer ratemaking of Cambridge's 13.8 kV facilities from transmission to distribution upon the reclassification of those facilities. Nor do the intervenors claim that the Companies' proposal would not result in the transfer of the FERC revenue requirement for the facilities at the time of the reclassification.[12] The arguments of the three intervenors that addressed the issue disputed the Companies' overall approach and assert that the transfer should be accomplished by reducing transmission rates in accordance with FERC ratemaking principles and increasing distribution rates in an amount determined under Department ratemaking principles (Attorney General Initial Brief at 13-14; MIT/Harvard Initial Brief at 12-14; TEC Initial Brief at 6-10).

[11] Further supporting the proposition that the ratemaking transfer is appropriately resolved in this merger case is that the heading of paragraph 2.18 of the Settlement Agreement is "Merger Impact on Transmission Rates." Moreover, for the reasons described above, the transfer of ratemaking must be coordinated with the consummation of the merger, which effectively requires that this merger case be the proceeding in which specifics of the transfer be established. There is no basis to infer into the Settlement Agreement that the Companies would have agreed to a gap in time between the implementation of the merger and the transfer and recovery of Cambridge's 13.8 kV facilities that were agreed to as part of the merger.

[12] The manner in which the Companies have proposed to compute the FERC revenue requirement for Cambridge's 13.8 kV facilities is described in Exhibit NSTAR-CLV-1, at 25-26, and an example is provided in Exhibit NSTAR-CLV-7. No party took issue with the fact that the calculation will accurately transfer the FERC transmission revenue requirement to distribution rates and the Companies will not repeat that description here (see NSTAR Electric Initial Brief at 24-25). As described herein, the dispute on this issue relates to whether this approach is appropriate.

The Attorney General contends that the Companies' ratemaking proposal does not conform to Department rate-setting precedent because the revenue requirement is not based on historical test-year data adjusted for known and measurable changes (Attorney General Initial Brief at 13-14).[13]

MIT/Harvard states that the Companies' proposal is not revenue neutral because FERC ratemaking treatment is different from that of the Department and that the revenue requirement calculated at the time of the reclassification will be higher than what it was on June 30, 2005 (MIT/Harvard Initial Brief at 13-14).

TEC claims that the Settlement Agreement is silent on the methodology for transferring ratemaking and does not require the transfer of the FERC revenue requirement to distribution rates, as proposed by the Companies (TEC Initial Brief at 7-8). TEC also argues that the revenue requirement under the FERC methodology would be different from a revenue requirement computed under Department rate-setting principles (id. at 7). TEC proposes that the Companies be permitted "to file a cost of service study for the 13.8 kV assets, consistent with the Department's regulatory requirements" and defer the transfer until the Department properly makes a determination of the revenue requirements, even if it means delaying the transfer until the end of 2007 (id. at 9-10).

The intervenors' criticisms of the Companies' ratemaking proposal for the transfer of Cambridge's 13.8 kV facilities from transmission to distribution miss a critical point: it is the only proposal that structurally complies with the no-net-harm standard for

13 Citing Boston Gas Company v. Department of Public Utilities, 367 Mass 92 (1975), it acknowledges that the Department may adopt the Companies' ratemaking proposal, as long as it explains why it has deviated from its traditional ratemaking precedent (id.).

Department review of mergers. The transfer of the revenue requirement that would have been collected in transmission rates to distribution rates ensures that customers (and the Companies) are no worse off than they would have been in the absence of the merger and the transfer of ratemaking for the 13.8 kV facilities. If transmission rates are reduced in accordance with the FERC formula rate, and distribution rates are increased by the different ratemaking calculation under Department procedures, there can be no assurance that customers (or the Companies) will be held harmless; it could result in either higher rates or lower rates for customers. The Companies' proposal ensures that neither customers nor the Companies gain or lose through the transfer (Exh. NSTAR-CLV-1, at 25; Exh. DTE-1-9; Tr. 3, at 403).

Not only is the Companies' proposal conceptually appropriate and consistent with the no-net-harm standard, the calculation of distribution revenue requirement could not be properly coordinated with the consummation of the merger, consolidation of transmission rates and reclassification of the Cambridge 13.8 kV facilities. As explained in Exhibit DTE-5-5, because the Department's ratemaking policies are based on an historical test year, it is not possible to compute a revenue requirement for a particular date until well after the fact:

> Given that the transfer of assets effectively takes place…at year-end 2006, preparing a revenue requirement calculation under Department precedent for January 1, 2007 would require a 2006 test year calculation and a post-2006 rate year, which includes known and measurable adjustments. Preparing a 2006 test year cost of service would be complex, and would include many assumptions that need to be reviewed and approved by the Department. Such a filing would be costly and would not be possible until some time in 2007. Moreover, even if that calculation could be performed, that revenue requirement could not be removed from the FERC transmission rates on a revenue-neutral basis, because the FERC rates are based on a formula that is calculated in a different manner.

The suggestion by TEC that the Companies could perform an isolated revenue-requirement calculation for the Cambridge 13.8 kV facilities (TEC Initial Brief at 9) misconstrues the nature of the calculation. It is not possible to compute a revenue requirement for specific facilities without performing a revenue-requirement calculation for the entire company (Exh. DTE-6-1 ("[w]ithout analyzing all expenses and accounts for that calendar year, there is no way to determine the expenses associated with the 13.8 kV facilities of Cambridge for that year")).

MIT/Harvard's suggestion that the Settlement Agreement limits the amount of the transfer to the $8.3 million revenue requirement computed for the Cambridge 13.8 kV facilities as of June 30, 2005 is likewise without merit and would severely penalize the Companies. MIT/Harvard points to nothing in paragraph 2.18 of the Settlement Agreement that implies that the transfer of ratemaking is linked to a revenue requirement that will be based on stale data, more than a year and one-half old. The operative language clearly looks to a time in the future, i.e., at the consummation of the merger (Settlement Agreement at ¶ 2.18 ("…Cambridge's 13.8 kV facilities shall be reclassified as distribution facilities and recovered in distribution rates…")). MIT/Harvard's suggestion to base the transfer on facilities in place on June 30, 2005 would have the effect of eliminating from the calculation the 50 percent increase in rate base resulting from the system upgrades in Cambridge and would deprive the Companies from recovering approximately $5 million per year (Exh. DTE-5-4). This penalty is neither equitable nor appropriate, and would deprive the Companies of a reasonable opportunity to earn a reasonable return on its investments.[14] The Companies could not go forward with the merger if such a penalty were imposed (Exh. DTE-2-12).[15]

Accordingly, the Companies have demonstrated that their proposal to transfer recovery of Cambridge's 13.8 kV facilities from transmission to distribution rates, consistent with the requirements of the Settlement Agreement, is reasonable, appropriate and meets the no-net-harm standard of Section 96. The intervenors' arguments are without merit and the Companies' ratemaking proposal should be approved by the Department.

3. The Proposed Changes to the Cambridge Standby Rates Are Reasonable, Appropriate and Meet the No-Net-Harm Standard.

As described in the Companies' Initial Brief, the transfer of recovery of Cambridge's 13.8 kV facilities in distribution rates will correspondingly result in an increase the standby contract demand portion of Cambridge's SB-G2 and SB-G3 standby rates (along with every other distribution rate) (NSTAR Electric Initial Brief at 26-28). No party has alleged that the Companies have improperly computed the change in

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14 Ironically, it is these same investments in Cambridge's 13.8 kV system that certain intervenors point to as necessary (and not having been completed fast enough) to reduce or eliminate congestion costs in Cambridge.

15 TEC complains that the Settlement Agreement did not contemplate that Cambridge could "apply the so-called 'Simplified Incentive Plan' ('SIP') (Rate Settlement Agreement, § 2.6) annually to a transmission-based revenue requirement" (TEC Initial Brief at 8). While it is true that inflation-related rate adjustments under the terms of the "SIP" provisions of the Settlement Agreement will apply after the 13.8 kV facilities are transferred, it is because they will no longer be considered transmission facilities and will be included in distribution prices (Tr. 3, at 302). It should also be noted that future SIP adjustments would not be significantly different from the annual increases that would otherwise be implemented under FERC's formula rate if 13.8 kV facilities, including future investment and increased O&M relating to 13.8 kV facilities (as affected by inflationary pressures), if those facilities were to continue to be considered transmission facilities and be subject to FERC ratemaking jurisdiction. If anything, because the SIP inflation offsets are far above those previously granted by the Department in litigated price-cap cases, it is likely that the annual SIP increase will be smaller than actual annual rate increases under FERC formula transmission rates.

standby rates associated with the proposed change in distribution rates. Two of the intervenors challenged the increase in the standby rates resulting from the change in the contract demand element of the charge (MIT/Harvard Initial Brief at 10-12; TEC Initial Brief at 7-12).

MIT/Harvard isolates the large percentage increases in individual rate elements of the Cambridge standby rates and claims that such percentage increases "in any existing rate is a serious public harm, one that, by itself, all but invalidates the Companies' claim that the merger meets the no net harm standard" (MIT/Harvard Initial Brief at 7). MIT/Harvard goes on to argue that such an increase in rates will tend to discourage new on-site generation and that no change in standby rates should be approved until the Department considers policy issues relating to distributed generation in the recently opened investigation in D.T.E. 02-38 (id. at 11-12).

TEC calls the increase in the Cambridge standby rates "the most problematic feature of the Companies' proposed merger" (TEC Initial Brief at 10). TEC also points to the percentage increases in rate elements of the Cambridge standby rates and criticizes the Companies' attempts, in response to a Department record request, to quantify the dollar impacts of the rates on a hypothetical standby customer (id. at 10-11).

The arguments regarding the impact of the change in Cambridge's standby rates that flow from the change in distribution rates are off the mark. For the following reasons they either misapply the no-net-harm standard or argue policy issues that are not pertinent to the outcome in this proceeding.

The issue of the percentage change in the contract demand portion of standby rates is not relevant to the no-net-harm standard since there can be no harm if no one is on the rate and there is therefore no increase being collected. The intervenors, correctly, have not attempted to allege customer harm where distribution rate increases to Cambridge's customers are offset by reductions in transmission rates. Similarly, any increase in the contract demand charges that could be imposed (without an offsetting rate reduction) could theoretically cause customer harm only <u>if any customers were taking service</u>. This is demonstrably not the case since Cambridge has entered into an amendment of the special contract with the single customer that arguably would be affected (RR-DTE-3(Supp)).

The isolated percentage change in the contract demand portion of the standby rates does not implicate the Department's longstanding concern about rate continuity because there is nobody taking service under the rate. The Department defines rate continuity as follows:

> Rate continuity means that changes to rate structure should be gradual <u>to allow consumers to adjust their consumption patterns in response to a change in structure</u>.

<u>Fitchburg Gas and Electric Light Company</u>, D.T.E. 02-24/25, at 252-253 (2002) (emphasis added). Obviously, if there are no customers taking service under a rate, there can be no concern about their ability to change consumption patterns. Moreover, even MIT/Harvard acknowledges, as the Companies' rate expert, Henry C. LaMontagne, pointed out during hearings, that the contract demand portion of a generator's total electricity costs is a relatively small percentage of the customer's overall energy cost (MIT/Harvard Initial Brief at 10). The record shows that decisions on any future large-scale on-site generation project that would be covered by the rate will be driven by the total economics of project (Tr. 2, at 232-234). Compared to other elements of a large customer's total energy cost, including most materially the price for generation (<u>i.e.</u>,

Basic Service rates), the contract demand portion of the standby rate is extremely small. Thus, the percentage change in the contract demand element of the Cambridge standby rate cannot create any harm to existing customers.[16]

On the "policy" issues raised about the generalized claims of a "disincentive" to distributed generation resulting from the higher standby rates in Cambridge, this case is not the proper forum to resolve such matters.[17] As noted by both MIT/Harvard and TEC, the Department has a pending proceeding in which it may consider such issues. In this case, the changes to the standby rates continue the existing Department policy and the existing rate design already in place for Cambridge, Boston Edison and Commonwealth under D.T.E. 03-121. The contract demand rate structure was adopted in compliance with a Department order approving a settlement agreement, which already includes numerous exceptions and reductions to fully compensatory standby rates. As the Department stated in its order D.T.E. 03-121:

> The Department's ratemaking policy requires cost responsibility to follow cost incurrence. [citations omitted] The cost to serve standby and continuous-use customers is the same [citations omitted], but the potential for rate recovery of the cost of service is quite disparate. The ability to recover costs from standby customers requires a different approach [citations omitted]. To comply with the Department's ratemaking policy, standby rates must be designed so that the costs of providing standby service are recovered from standby customers and not shifted to other customers. Use of monthly metered demand charges will not allow the

16 As noted in the Companies' Initial Brief, to avoid any allegations that a prospective on-site generator has already made commitments based on the existing levels of contract demand, the Companies would agree to delay the implementation of the resulting standby rate for any customer that develop projects before June 30, 2007 (NSTAR Electric Initial Brief at 29, citing RR-DTE-3).

17 One would assume that the intervenors would agree that an uneconomical incentive resulting from an inordinately low contact demand rate would also violate public policy. In that context, it should be noted that, even with the estimated increase for Cambridge, the standby distribution rate of approximately $2.70 per kVa for a contract demand under 1,000 kVa and $3.70 per kVa for a contract demand over 1,000 kVa are significantly lower than the corresponding levels for Boston Edison. See Tariff No. M.D.T.E. 190, Rates SB-G3 and Rate SB-T2, on file with the Department.

> distribution company to recover costs incurred to provide the local distribution facilities needed to "stand by" for the DG customer [citation omitted].

NSTAR Electric, D.T.E. 03-121, at 46-47 (2004). Until and unless the Department changes its ratemaking policies with regard to standby rates, failure to make the adjustments to Cambridge's standby rates would contravene public policy and would be inconsistent with the public interest/no-net-harm standard for approval of mergers.

Accordingly, the changes to the standby rates necessitated by the transfer of Cambridge's 13.8 kV facilities to distribution rates are reasonable, appropriate and comply with the statutory standard.

E. Other Issues

1. The Companies' Proposal to Consolidate Depreciation Rates Is Reasonable and Meets the No-Net-Harm Standard.

The Companies' Initial Brief contained a detailed summary of the manner in which NSTAR Electric proposes to comply with the requirements of paragraph 2.6.2 of the Settlement Agreement approved in D.T.E. 05-85 regarding the expense-neutral consolidation of depreciation rates (NSTAR Electric Initial Brief at 28-35, citing Exh. NSTAR-CLV-1, at 29-36; Exh. NSTAR-CLV-9; Exh. NSTAR-CLV-10, as revised; Exh. NSTAR-CLV-11; Exh. DTE-1-25; Exh. DTE-2-3; Exh. DTE-2-5; Exh. DTE-4-1; Exh. DTE-4-11). As demonstrated by the record in this case, the Companies' depreciation proposal comports with the requirements of the Settlement Agreement, and the Companies will not repeat the arguments contained in the Initial Brief. The Attorney General raises two issues relating to the proposal, which will be addressed below. No other intervenor addressed depreciation on brief.

The Attorney General argues that the Companies' proposal to amortize (rather than depreciate) certain general plant equipment is not expense-neutral (Attorney General Initial Brief at 17-18). As described in the Companies' Initial Brief, this change in the accounting procedures is intended to implement the terms of FERC Accounting Release No. 15, which permits this more simplified accounting procedure for certain high-volume, low-dollar-value accounts (NSTAR Electric Initial Brief at 33-36). The Attorney General contends that the proposed 15-year amortization, or 6.67 percent per year (1/15 = 6.67), which the Companies would apply for new equipment in the specified general plant accounts, would lower the depreciation expense from the 7.5 percent annual accrual rate proposed for existing equipment in these accounts. According to the Attorney General, the annual accrual rate for these general plant accounts should be 7.5 percent to maintain expense neutrality (Attorney General Initial Brief at 17-18).

The Companies agree and will amortize the relevant accounts at an annual rate of 7.5 percent (or an amortization period of approximately 13.33 years).[18]

The Attorney General also requests that, if the Department approves the depreciation consolidation proposal, it should also order NSTAR Electric "to maintain plant installation, retirement, cost of removal, salvage value, depreciation expense, and accumulated depreciation data at the plant account/subaccount level" (id. at 18). Presently, Boston Edison keeps its depreciation records at the functional level rather than

[18] The Attorney General also implies that the accounting change is not in compliance with the depreciation-rate-consolidation provisions of the Settlement Agreement (id. at 18). The Companies disagree. As noted by the Attorney General, the Settlement Agreement is silent on this issue. The Settlement Agreement does not prevent this type of accounting change as long as the consolidation of depreciation rates is expense-neutral. With the agreed change to the annual amortization rate, the Companies' proposal for the consolidation of depreciation rates is expense-neutral in compliance with the terms of the Settlement Agreement.

the plant account level. The Companies' proposal includes the maintenance of all depreciation at the plant account level as requested by the Attorney General. No further action on this issue by the Department is necessary.

2. Disallowance of SCR/RMR Costs Associated with Cambridge 13.8 kV Project Is Outside the Scope of this Proceeding.

In a remarkable example of over-reaching, TEC proposes that Department approval of the merger should be conditioned on NSTAR Electric "agreeing to shoulder the SCR/RMR costs associated with delay in the installation of the Putnam Line beyond May 1, 2006 and all associated construction costs in excess of the original $11.4 million estimate" (TEC Initial Brief at 21). Those ratemaking issues are not before the Department at this time, and must be summarily rejected by the Department in this case.

Essentially, TEC is asking the Companies to concede that any delay, cost over-runs or costs imposed by third-party generators, the ISO-NE and/or FERC be borne by the Companies' shareholders without regard to assessing issues of fault, prudence, damages, jurisdiction or due process.[19] The record in this case does not even begin to deal with these issues, nor should it, since they are outside of the scope of this merger case. The Companies will not take the bait and debate TEC's unsubstantiated allegations. Such an unacceptable and unrelated "condition" for approval of the merger proposed in compliance with the terms of the Department-approved Settlement Agreement in D.T.E.

[19] TEC apparently believes that shareholders can be liable for all costs based on a theory of strict liability. Even if this were the legal standard, which it isn't, the Companies must be afforded due-process rights to defend themselves before their property can be appropriated by government action.

05-85 cannot be seriously considered by the Department.[20]

3. Further Extension of the Energy Efficiency Agreement with CLC Is Outside the Scope of this Proceeding.

CLC expresses a concern that the Companies will not collect and maintain data as required under the existing agreement between CLC and Commonwealth relating to the provision of energy efficiency services (CLC Initial Brief at 15). Although the Companies have stated that they will continue to honor their contractual obligations (Exh. CLC-1-26), CLC requests that the Department condition the approval of the merger on the Companies extending the existing contract through "at least December 31, 2010" (id.).

Conditioning approval on an extension of the contract is inappropriate and should be rejected by the Department. The issue of the provision of energy efficiency services is outside the scope of this proceeding and not affected by the merger. There is no record evidence in this case about the referenced contract (other than the fact that the Companies will comply with existing obligations), and any future contractual arrangements will be addressed by the parties, when appropriate. Department intervention in this process is inappropriate at this time, and certainly cannot be addressed in this case and in the absence of record evidence. CLC's argument is without merit, and the Department must decline to impose the requested condition.

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[20] Similarly, TEC's request that approval of the merger be conditioned on the immediate refund of reduced RMR costs associated with the Kendall Generating Station (TEC Initial Brief at 22) is outside the scope of this proceeding. Transmission cost changes will be handled as part of the normal reconciliation process.

4. Sharing of Merger Benefits Is Fair and Meets the No-Net Harm Standard.

CLC argues that "…NSTAR shareholders will receive a disproportionate benefit that will result from efficiencies achieved through the [m]erger…" which should be shared with customers (CLC Initial Brief at 15). For the following reasons, CLC's contention is incorrect, and the merger benefits will properly accrue to customers.

The record is clear that the merger meets the no-net-harm standard and that customers will receive significant benefits. The immediate and quantifiable costs and benefits are not large: approximately $600,000 in costs to be borne by shareholders for outside legal expenses and information technology changes (Exh. DTE-3-5) and approximately $400,000 in annual administrative cost savings (Exh. DTE-3-4). Although both figures are de minimis in the context of the entire revenue requirement of the Companies, some of the administrative savings will be allocated to transmission functions and be passed through to customers in transmission rates, and the distribution portion will be included in the revenue requirement in any future rate cases. However, many of the other, non-quantifiable savings resulting from the merger will flow directly to customers. For example, any reductions in the cost of Basic Service supplies resulting from larger procurements will result in lower Basic Service rates for customers (id.). Similarly, any improved customer service, reduction in rate confusion, and enhanced regulatory oversight will provide customer benefits (id.).

As the Companies have stated on numerous occasions in these proceedings, customers have already received the hundreds of millions of dollars in benefits of the merger that created NSTAR (Exh. NSTAR-CLV-1, at 9-10; Exh. DTE-2-1; see also Attorney General Initial Brief at 3). The costs and benefits of this final step in the corporate reorganization are, in comparison, modest, and the Companies have not alleged otherwise. Nonetheless, the benefits will flow to customers and there is no need to establish an explicit savings tracking or sharing mechanism (which would likely cost more than the administrative savings). The CLC proposal should be rejected.

III. CONCLUSION

The Companies have demonstrated on this record that their proposal to implement the corporate merger that will create a single NSTAR Electric Company complies with the applicable statutory standard and Department precedent. The formal merger of the Companies will further streamline administrative and regulatory operations, reduce customer confusion, improve customer service and complete the business restructuring contemplated by the creation of NSTAR (D.T.E. 99-19) and endorsed in the Settlement Agreement approved by the Department in D.T.E. 05-85.

Intervenors in this proceeding have often tried to misapply the legal standard of review and/or have presented arguments on issues that are outside of the scope of this case. The Companies acknowledge the fact that the vast majority of merger savings were attained through the creation of NSTAR and the realization of operational efficiencies. However, additional benefits (albeit some difficult to quantify) are possible through the proposed merger of the Companies, and customers "would be at least as well served by approval of [the] proposal as by its denial." D.T.E. 99-19, at 10 (1999). As described above, the objections raised by the intervenors are without merit, and the Companies have demonstrated that their merger proposal is in public interest in that it will result in no net harm (and will indeed create net benefits).

Accordingly, based on this record, the Department should approve the proposed merger pursuant to G.L. c. 164, § 96 and determine that that the proposed merger and the terms thereof (including the proposed rate consolidations, the proposed establishment of uniform depreciation rates and the reclassification and the proposed transfer of Cambridge's 13.8 kV facilities to distribution rates) are consistent with the public interest. In addition, the Department should confirm that Boston Edison (to be renamed NSTAR Electric Company), as the surviving corporation of the merger among and between the Companies, will continue to have all of the franchise rights and obligations that were previously held by Cambridge and Commonwealth, and that further action, pursuant to G.L. c. 164, § 21, is not required to consummate the merger,

Respectfully submitted,

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CAMBRIDGE ELECTRIC LIGHT COMPANY
COMMONWEALTH ELECTRIC COMPANY
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